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IN THE

Supreme Court of the United States

October Term, 1953

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No. 382

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NORTHERN NATURAL GAS COMPANY,
Petitioner,

v.

FEDERAL POWER COMMISSION,
Respondent.

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REPLY TO FEDERAL POWER COMMISSION'S AND INTERVENERS' BRIEFS IN OPPOSITION TO PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE EIGHTH CIRCUIT

o———o———o

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Petitioner, Northern Natural Gas Company, hereinafter undertakes to reply to the Federal Power Commission's Brief in Opposition[1] and to the Interveners' Brief in Opposition,[2] and respectfully brings to the attention of the Court the following:

STATEMENT OF FACT

In the Brief in Opposition of the Federal Power Commission, it is stated (F.P.C. Br. p. 4, footnote 1) that with respect to Petitioner's third rate filing of December

1 Hereinafter referred to as "F. P. C. Br."

2 Hereinafter referred to as "Int. Br."

26, 1951 (R. VI 2438), "no additional questions as to this filing are raised in the petitions for certiorari." Petitioner wishes to note that, while no *additional* questions are presented by the third rate filing, the issues as to which Petitioner seeks review in this Court in the first two rate filings are present in and common to the third rate filing (Pet. in No. 382, p. 1) and, therefore, the issues and Petioner's damage continue through the time the rates contained in the third filing are effective.

The Commission, based on the assumed correctness of its Opinion No. 228 with respect to Petitioner's first two rate filings, issued its Opinion No. 233 in Petitioner's third rate filing, dismissing Petitioner's contentions on the issues that are the subject of the Petition for Certiorari in case No. 382 (Pet. in No. 382, pp. 6-7). Based upon the fact that common issues were present and Petitioner's damage continues through the the entire time the rates contained in the third filing are effective, the Court below stayed Opinions Nos. 228 and 233 pending review (R. VI 2415-2420) and by Order dated September 15, 1953 (Appendix A, pp. 17-19, infra) such Court stayed the issuance of its Mandate and continued such Stay Order in effect pending this Court's determination of the issues in cases Nos. 381 and 382.

ARGUMENT IN REPLY

Question I

(a) The "end result" doctrine is not applicable to the question presented.

The idea is presented that the Supreme Court may properly decline to review the issue as to the effect of the Kansas 8-cent attribution order if it feels that the "end result" of the rates fixed by the Commission is just and reasonable (F.P.C. Br. p. 11; Int. Br. p. 14). It is stated that

this Court "is not concerned with the method used by the Commission in reaching its result." The cases cited, however, do not involve any such factors as are present in the instant case where a State agency has acted within the admitted scope of its jurisdiction setting up, as a conservation measure, a condition precedent to the production of gas from a common reservoir located in the state, which condition has been ignored by the Federal Commission in fixing rates subject to its jurisdiction. The issue in the instant case is not, therefore, the effect to be given an ordinary administrative action affecting only the regulatory theories of the administrative body and the contentions of a party subject to regulation. The issue presented here involves the conflict between the conservation efforts of a state and rate regulation by a federal agency.

Under the circumstances in this case the "end result" doctrine is clearly inapplicable since the question for determination is the effect and application that the Federal Power Commission, in fixing resale rates of Petitioner, must (or should) give to the conservation order of the Kansas Commission.

The Interveners state that the question presented "really" is: "Is Federal power superior to the power of a state in the interstate rate-making field?" (Int. Br. p. 15). Such a statement is not worthy of an answer. Petitioner has nowhere asserted that the states have any power to fix rates for sales of natural gas for resale in interstate commerce (except to the extent that §1(b) of the Natural Gas Act reserves such power to the states). Petitioner's position stated in its simplest form is that the Federal Power Commission must (or in the exercise of its discretion should) recognize the minimum well-

head conservation price fixed by the Kansas Commission as a "floor" in determining Petitioners rates,

(b) **Petitioner's contention is not a claim for "fair field price" for the gas it produces in the Kansas Hugoton Field.**

It is stated that Petitioner's contention with respect to the Kansas conservation order "is in effect merely a revival—and indeed an extension—of the 'fair value' argument which the Commission, with this Court's approval, has consistently rejected" (F. P. C. Br. p. 12). Petitioner repeats that its claim in this regard is not a claim for "fair field price" or "fair value." Commissioner Smith in his concurring opinion recognized this when he said (R. V 2307):

> Northern does not contend that this state-fixed minimum price represents the commodity value of the gas which it produces in the Hugoton field, where in fact current sales of gas have been made at somewhat higher prices.

As stated in the Petition for Certiorari in this case, the fair or actual value of the gas in question was not less than 10 cents per Mcf (R. I 200-202, 210-214, III 1479-1484). Petitioner reiterates that its claim is a conscientious effort to effectuate the requirements of the state conservation order (Pet. in No. 382, p. 21).

(c) **"Settled principles" are not decisive of this new question.**

The argument is made that since the Commission followed "settled principles," the case should not be reviewed (F.P.C. Br. p. 13; Int. Br. pp. 16-17). Such a contention begs the question. The question presented and to be determined concerns the effect of the Kansas conservation order on those principles. That question

cannot be said to be settled since it has never been presented to this Court.

(d) **The doctrine of "federal supremacy" is neither applicable nor controlling.**

The Federal Power Commission asserts that the question of its action conflicting with the conservation order of the Kansas Commission can be resolved by the application of "elementary principles of federal supremacy" (F. P.C. Br. p. 14). Such principles are neither applicable nor controlling. The state regulation here involved concerns conservation of natural gas, a field from which Congress has specifically excluded federal authority, viz., the "production or gathering" of natural gas (Natural Gas Act, §1(b)). Since the federal authority has not been extended to conservation of natural gas it cannot be supreme to the authority of the state in such field. Furthermore, the doctrine of "federal supremacy" should only be applied if state and federal regulation with respect to a subject matter cannot reasonably stand together. Here the regulation of the Federal Power Commission and the Kansas Commission conflict only because of the arbitrary application by the Federal Commission of a "utility cost formula" to Petitioner's Kansas Hugoton Field production.

(e) **Petitioner's rates, as determined by the Federal Power Commission, conflict with the Kansas conservation order.**

Both the Federal Power Commission (F.P.C. Br. pp. 6 and 15) and the Interveners (Int. Br. p. 7) intimate that there is no conflict between Petitioner's rates as determined by the Federal Power Commission and the Kansas conservation order.

The first ground presented for the theory of a lack of conflict is that since the rates fixed provide for charges in excess of 8 cents per Mcf, at delivery points hundreds of miles away from the wellhead, the Kansas wellhead conservation order has been recognized by the Federal Commission. Judge Johnsen in his concurring opinion in the Court of Appeals (R. VI 2496) indicated that that was the basis of his concurrence. He goes on to state, however, that the conclusion "is more escapive than satisfying" (R. VI 2497). With this statement, Petitioner is wholly in accord. If the Kansas conservation order is to be given any effect, the terms of the order must be given their logical and ordinary meaning. The Kansas order provides for the attribution of 8 cents *"at the wellhead."* The Kansas Commission acted within the scope of its jurisdiction in regulating the production and gathering of gas within the State of Kansas by fixing a minimum wellhead conservation price. The Federal Power Commission is, therefore, confronted *at the wellhead* with a condition of production created by the valid exercise of state power. The Federal Power Commission allowed only the accounting costs of Petitioner's production of Kansas Hugoton field gas—aproximately 5 cents per Mcf—as the *wellhead* price of the gas (R. VI 2453). Obviously, what the Federal Power Commission in effect ordered as the *wellhead* price of gas does not permit Petitioner to comply with the Kansas conservation order. The mere fact that at some point far distant from the Kansas gas field, and after accounting for costs of transportation, a charge in excess of 8 cents per Mcf is collected does not constitute compliance with the minimum *wellhead* conservation price.

The second ground suggested as to why there is no conflict between the Kansas order and the Federal Power

Commission's rate-fixing order is that the particular Kansas order has not been reviewed by the Courts of Kansas (F.P.C. Br. p. 15). This factual situation was clearly shown in the Petition for Certiorari in No. 382 (pp. 8-9). The order reviewed by the Kansas Supreme Court was an Interim Order and was slightly different in form than the order later issued. The terms of the Kansas Order, however, which is the basis of Petitioner's contention in this regard are clear. The Chairman and General Counsel of the Kansas Commission testified and stated that an allowance by the Federal Power Commission of 8 cents per Mcf at the wellhead was necessary to comply with the Kansas Order (R. I 234-249, 253-256). To say that the Kansas conservation order here involved might possibly be construed by the Kansas Supreme Court in such a way as to resolve the conflict between the State Commission and the Federal Commission is to grasp at a straw to avoid the decision of this Court. The provisions of such conservation order are entirely consistent with the holding of this Court that "the connection between realized price and conservation applies to all production in the field" (*Phillips Petroleum Co. v. Oklahoma*, 340 U. S. 190, 192).

(f) **The issue of whether the Federal Power Commission abused its discretion is properly before this Court.**

With regard to Part B of Question I in the Petition for Certiorari in No. 382 (pp. 2-3), it is the contention of the Federal Power Commission that Petitioner did not claim such Commission should give effect to the Kansas Order as a matter of discretion (F.P.C. Br. p. 16). Admittedly, Petitioner did and does maintain as its primary contention that the Federal Power Commission is legally bound to give effect to the Kansas Order. As an alternative position, however, Petitioner has maintained ever

since its Application for Rehearing before the Federal Power Commission (after it first learned the position of the Commission) that if the Federal Commission is not legally compelled to give effect to the State Order it *should* recognize it because otherwise, as stated in the Application for Rehearing before the Commission, the action of the Federal Power Commission is erroneous for the reasons that it (R. V 2360-2361):

> * * * disregards the legitimate local interest of the state in a field where the state has the paramount authority, by nullifying the justifiable action of the Kansas Corporation Commission to effect conservation of an irreplaceable natural resource; substitutes accounting cost "conventions" for an allowance of a conservation price of 8¢ per MCF to Northern for its Kansas Hugoton Field production and thereby attributes to Northern's production at the wellhead in such field a value and allowance per MCF equal only to the accounting costs associated with production, in violation of the conservation order of the Kansas Corporation Commission; fails to allow Northern as cost of service a price of 8¢ per MCF at the wellhead for Northern's Kansas Hugoton Field production or as an alternative fails to allow Northern as cost of service the market value for such production which would equal or exceed in amount the 8¢ per MCF at the wellhead fixed by the Kansas Corporation Commission; arbitrarily substitutes accounting cost theories for equity and sound economic considerations by the application of a so-called "utility rate making" theory to the production of natural gas which is a non-utility function, all of which is contrary to the record and the present and the future public interest; fails to comply with the provisions of the Federal Administrative Procedure Act, Section 8(b) (5 U.S.C.A. 1008), in that the Commission fails to set forth the reasons or basis for finding and concluding as above quoted with respect to the

> material issues of law presented; and, is arbitrary, capricious and otherwise not in accordance with the law.

That the issue of whether the Federal Power Commission *should* have given effect to the Kansas Order was before the Commission and was considered by it is shown by the dissenting opinion of Commissioner Wimberly (R. V 2311-2314), wherein it is stated (R. V 2312):

> The question is not, as has been inferred, that this Commission is asked to submit to the Kansas order in fixing the interstate rates of Northern Natural. I do not think it is too much to expect that the federal agency give proper weight to the state order when it is made abundantly clear it applies to all gas produced in the Kansas Hugoton field, whether such gas is consumed locally or in distant interstate markets.

Commissioner Smith, concurring separately, states (R. V 2309):

> This of course does not mean that this Commission would be without authority, in the exercise of its own discretion, to consider and weigh the lawful actions of duly constituted State authorities. On the contrary, if the Commission were, in a proper case, to follow what I think would be a more realistic approach to the treatment of pipeline-produced gas for rate-making purposes, it could—and I should hope that it would— give great weight to, among other factors, the minimum prices established for gas by State agencies close to and fully familiar with local conditions in the producing areas.

The issue was raised by this Petitioner in its Petition for Review filed in the Court of Appeals (R. I 19-20); was clearly presented to and argued before that Court in Petitioner's Main Brief (pp. 60-61 thereof, reproduced as Appendix B herein, pp. 20-21, infra), in Petitioner's Re-

ply Brief (pp. 22-26 thereof, reproduced herein as Appendix C, pp. 22-26, infra), and in the oral argument before the Court (transcript of oral argument, pp. 70-73).

Raising the issue in the Application for Rehearing clearly preserves it for the consideration of this Court. A similar situation existed in the case of *City of Yonkers v. United States,* 320 U. S. 685. There this Court stated (320 U. S. 685, 688):

> The Commission says that the question of its jurisdiction under §1(22) was neither presented in limine nor urged in the briefs, in the exceptions to the examiner's report, or in the oral arguments. It was, however, presented in petitions for reconsideration which the Commission denied without opinion.

This Court held the point was properly preserved for its consideration.

The Federal Power Commission has determined only (and Petitioner submits erroneously so) that it is not compelled to give effect to the Kansas conservation order. It fails or refuses to exercise its discretion so as to enforce the intent of the Natural Gas Act "to complement and in no manner usurp State regulatory authority" (See *Interstate Natural Gas Co. v. F. P. C.,* 331 U. S. 682, 690, quoting the House Committee Report). Further it does so without reasons or explanation.

The situation presented here in this regard is not unlike that discussed in *Phelps Dodge Corporation v. N. L. R. B.,* 313 U. S. 177.[2a] There this Court stated (313 U. S. 196):

> Thus the Board determined only the dry legal question of its power, which we sustained; it did not consider whether in employing that power the policies of the Act would be enforced.

2a Specifically cited in the Legislative History, Administrative Procedure Act, as a reason for including the second sentence in §8(b), to require statements of "why" discretion is so exercised

The Court said that the Board ordered reinstatement "merely because it asserted its legal power so to do" (313 U. S. 197) but complained that it could not "really tell why the Board has ordered reinstatement" (313 U. S. 196). The case was remanded to the Board, this Court stating (313 U. S. 197):

> * * * it will avoid needless litigation and make for effective and expeditious enforcement of the Board's order to require the Board to disclose the basis of its order. We do not intend to enter the province that belongs to the Board, nor do we do so. All we ask of the Board is to *give clear indication that it has exercised the discretion with which Congress has empowered it.* (Emphasis supplied)

Certainly the same considerations are present in the instant case. Here the Commission determines only that it is not compelled to give effect to the Kansas Order but gives no indication why it should not give effect to such order, thereby complementing the State regulatory authority. In the field of federal-state relationships such as are here involved, it is not only appropriate but legally necessary that a federal administrative body exercise its authorized discretion. What this Court and this Petitioner are entitled to is that the Commission "give clear indication that it has exercised the discretion with which Congress has empowered it."

(g) The Commission opinion, refusing to give effect to the Kansas conservation order, is devoid of findings and conclusions, as well as the reasons or basis therefor, on material issues of law and discretion.

With respect to the failure of the Commission to state the reasons why it acted as it did, the Commission admits in its Brief (F.P.C. Br. p. 16) that "the prevailing opinion of the Commission brushed Northern's contention

aside with a minimum of discussion." To mitigate this serious deficiency the Commission points to the discussions set out in the two divergent concurring opinions as satisfying the requirements of the Administrative Procedure Act, §8(b). Such a contention merely raises the further substantial federal question—will the requirement of Section 8(b) of the Administrative Procedure Act (5 U.S.C. §1007(b)) that "all decisions * * * shall * * * include a statement of (1) findings and conclusions, as well as the reasons or basis therefor, upon all the material issues of fact, law, or discretion presented on the record" be satisfied by reasons and bases set forth in two divergent concurring opinions? Obviously such requirement cannot be so satisfied in the instant case. From Commission Opinion No. 228 (R. V. 2264-2266) neither Petitioner nor this Court can determine why the *majority* refuses to give effect to the Kansas conservation order. Petitioner again calls the Court's attention to the fact (Pet. in No. 382, p. 24, footnote 27) that four Commissioners participated in the Commission decision on this issue. Two wrote divergent concurring opinions, one strongly dissented, leaving only the one remaining Commissioner as subscribing to the "reasons" set out in the majority opinion.

Aside from the question of the legal sufficiency of requiring this Petitioner and the Court to choose between divergent concurring opinions to find a basis or reason for the Commission decision, as the Commission suggests, it is Petitioner's contention that all the opinions considered together do not afford an adequate basis for the Commission action. In this connection, the instant case is not unlike the case of *City of Yonkers v. United States*, 320 U. S. 685, where there was involved the question of the authority of the Interstate Commerce Commission to

allow a carrier to abandon certain portions of its railroad line. By statute[3] the authority of the Commission to allow abandonment "shall not extend" to certain street, suburban, or interurban electric railways. The Interstate Commerce Commission in authorizing the abandonment in question did not discuss the limitations on its authority as set out in Section 1(22).

On appeal to this Court from a ruling by a three-judge District Court in favor of the I. C. C., this Court reversed, stating (320 U. S. 692):

> We are asked to presume that the Commission, knowing the limit of its authority, considered this jurisdictional question and decided to act because of its conviction that this branch line was not exempt by reason of §1(22). But that is to deal too cavalierly with the Congressional mandate and *with the local interests which are pressing for recognition. Where a federal agency is authorized to invoke an overriding federal power except in certain prescribed situations and then to leave the problem to traditional state control, the existence of federal authority to act should appear affirmatively and not rest on inference alone.* (Emphasis supplied)
>
> This is not to insist on formalities and to burden the administrative process with ritualistic requirements. It entails a matter of great substance. It requires the Commission to heed the mandates of the Act and to make the expert determinations which are conditions precedent to its authority to act.

An analogous situation is presented in the case at bar in that the specific exclusion of Commission jurisdiction from "production and gathering"[4] is nowhere mentioned

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3 Section 1(22) of the Interstate Commerce Act, 49 U. S. C. §1(22).

4 Section 1(b) of the Natural Gas Act, 15 U. S. C. §717(b).

in the majority opinion or in the two separate concurring opinions. There is no way of knowing whether the Commission considered Section 1(b) of the Natural Gas Act, or of knowing how the Commission construes that section if it did give consideration to it. In this case, as in the *City of Yonkers* case, "we are asked to presume that the Commission, knowing the limit of its authority, considered this jurisdictional question and decided to act." Here, too, such a presumption deals "too cavalierly with the Congressional mandate and with the local interests which are pressing for recognition."

Question II

With respect to the question of allocation of costs, Petitioner challenges the Commission's failure to set forth any discussions, conclusions, or findings in respect to its classification of property taxes,[5] and challenges the substantiality of the evidence supporting the classifications of depreciation and property taxes.

With respect to the Commission's failure to support its classification of property taxes, the frank admission that such classification was not discussed in its Opinion obviates the need for further reply.

In respect to substantiality of evidence the only record evidence supporting the classifications made with respect to depreciation and property taxes is that of a Commission Staff *engineer's* theories of *equity*. The Federal Power Commission now says that such classifications were based on "practical reasons drawn from [the Commission's] experience in the field, and not on an engineer's theory of equity" (F.P.C. Br. p. 19). Suffice it

5 The Commission admits that its classification of property taxes was not discussed in its Opinion (F. P. C. Br. p. 20).

to say that the Commission's "practical reasons" are not record evidence in this case. Petitioner challenges the substantiality of the evidence presented on the record. To substitute "experience" for *competent factual* record evidence is to ignore the fact that every "natural gas company" necessarily presents a different factual picture to be considered by the Commission. The decision of the Commission must be based on the factual situation presented by a particular natural gas company in a particular phase of its development. The Commission Staff engineering witness who testified in this proceeding had or should have had all the knowledge that reasonably could be obtained about Petitioner and its operations. With his background of investigation of Petitioner's business, his record evidence which was to constitute the "substantial evidence" necessary for the Commission's decision consisted solely of his theories of "equity" (R. I 456-457, 506-507). Petitioner reiterates that such evidence is not "substantial evidence" within the meaning of Section 10(e) of the Administrative Procedure Act, 5 U. S. C. §1009(c).

Questions III and IV

With respect to questions III and IV, neither the Federal Power Commission nor the Intervener Respondents have set forth any matters that should defeat the Petition for Writ of Certiorari on these questions.

As a matter of the Court's convenience in considering these questions, however, Petitioner directs the Court's attention to the fact that each of the rate schedules involved (IND-1 and IND-2) is a separate and distinct rate schedule involving resale sales in the case of one (IND-1) and direct sales in the case of the other (IND-2) and, therefore, each presents a separate and distinct legal problem. Throughout the entire course of these proceedings, both

before the Commission and the Court below, there has been a lamentable tendency to consider the two rate schedules as presenting essentially one problem and to slur over the distinct legal difference in the questions presented by each.

CONCLUSION

No reasons have been advanced in the Briefs in Opposition which detract from Petitioner's position as set out in the Petition for Writ of Certiorari in No. 382. The Writ should be granted.

Respectfully submitted,

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November, 1953

APPENDIX A

UNITED STATES COURT OF APPEALS FOR THE EIGHTH CIRCUIT

September Term, 1953
Tuesday, September 15, 1953

No. 14704

State Corporation Commission of the State of Kansas,
Petitioner,

vs.

Federal Power Commission.

No. 14706

Northern Natural Gas Company, a Corporation,
Petitioner,

vs.

Federal Power Commission.

No. 14733

Northern Natural Gas Company, a Corporation,
Petitioner,

vs.

Federal Power Commission.

No. 14743

Northern Natural Gas Company, a Corporation,
Petitioner,

vs.

Federal Power Commission.

Petitions to Review Orders of Federal Power Commission.

ORDER

Before Judges Sanborn, Woodrough and Johnsen, Circuit Judges.

On Consideration of the separate motions of the Northern Natural Gas Company and the State Corpora-

tion Commission of the State of Kansas to stay mandate and continue in effect previously issued stay order pending application to the Supreme Court for a writ of certiorari, the separate resistances to such motions by the Federal Power Commission and by certain Interveners, the separate motions of the Federal Power Commission and certain Interveners to dissolve such previously issued stay, and the motion of certain Interveners for an order of refund to Interveners of amounts collected from them under the stay order, as well as the various showings of the several parties in relation to each of these matters.

IT IS ORDERED:

(1) That the motions of Northern Natural Gas Company and State Corporation Commission of the State of Kansas for stay of mandate in relation to the decision of this Court on the merits of the case be and hereby are granted, and that such mandate is hereby accordingly stayed until October 3, 1953, or, if on or before that date there is filed with the Clerk of this Court the certificate of the Clerk of the Supreme Court showing that petition or petitions for certiorari, record and supporting brief have been filed by Northern Natural Gas Company and State Corporation Commission of the State of Kansas, then such stay of mandate shall continue in effect until the issuance of mandate by the Supreme Court in the case.

(2) That the stay of the order of the Federal Power Commission, heretofore granted shall be permitted to remain in effect, in its present form and upon its present conditions, until October 3, 1953, or, if petition for certiorari is duly filed before that time, then until the ruling by the Supreme Court upon such petition.

(3) That upon a ruling by the Supreme Court on the petition for certiorari as aforesaid, either granting or

denying the same, any of the parties hereto may make application to this Court for vacation or modification of the stay order, as may be appropriate in relation to the certiarori ruling, and jurisdiction is hereby reserved to make such order of vacation or modification as shall seem to the Court at that time to be appropriate.

(4) That in all other respects the various requests of the several parties are hereby denied.

September 15, 1953.

APPENDIX B

Excerpts (pp. 60-61) from Northern Natural Gas Company's (Petitioner's) Main Brief in the Court of Appeals for the Eighth Circuit in Cases Nos. 14704, 14706, and 14733—the cases as to which review is sought in this Court:

Even if we assume, arguendo, that the Commission is not required by law to recognize the conservation order of the State of Kansas in fixing rates in connection with production owned by a natural gas company whose rates it regulates (which assumption Petitioner specifically denies) how can the Commission argue or deny, in view of statements such as the foregoing, that their denial of Petitioner's claim for attribution is anything other than arbitrary, capricious and a most serious abuse of administrative discretion and, therefore, erroneous as a matter of law?[27] Most certainly it cannot be argued that the Commission is compelled to disallow Petitioner's claim for attribution. Absent compelling reasons outside the Natural Gas Act, such as the Kansas Commission's conservation order, the Commission is not bound for rate-making purposes "to the service of any single formula or combination of formulas." See *F. P. C. v. Natural Gas Pipe Line Co.*, 315 U. S. 576, 586, 61 S. Ct. 735, 743 (1942).

In the light of the decisions of the *Cities Service* and *Phillips* cases, supra, upholding, without qualification, the authority of state regulatory bodies over production of gas, including fixing a minimum attribution price in

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27 See Federal Administrative Proceedure Act, Section 10(e) (5 U. S. C. §1009 (e)) providing that the reviewing court shall "hold unlawful and set aside agency action, findings and conclusions found to be (1) arbitrary, capricious, an abuse of discretion, or otherwise not in accordance with law * * *."

the interest of conservation, it seems unmistakably clear that such power being granted, and validly exercised, it must then, as a matter of law, be recognized by the Federal Power Commission for rate-making purposes and reflected in rates fixed by such Commission and ultimately in consumer rates. As pointed out above, an examination and consideration of public interest makes this conclusion inevitable.

APPENDIX C

Excerpts (pp. 22-26) from Northern Natural Gas Company's (Petitioner's) Reply Brief in the Court of Appeals for the Eighth Circuit in Cases Nos. 14704, 14706, and 14733—the cases as to which review is sought in this Court:

2. Assuming arguendo, absence of such legal compulsion, the Commission's refusal to include this attribution price in the fixing of Petitioner's rates is arbitrary, capricious and an abuse of discretion and on this ground should be reversed.

Even if it be assumed, solely and exclusively for the purpose of argument, that the Commission as a technical legal proposition is not compelled to allow as a part of the city gate rate the wellhead conservation or floor price fixed by the Kansas Commission, the refusal to allow the 8c wellhead price on the facts of the instant case is arbitrary, capricious, unreasonable and an abuse of discretion and, under the standards of the Administrative Procedure Act, warrants reversal on that ground alone (Pet. Br. pp. 59-61).[38]

Relying on several court expressions, the Commission has repeatedly reasserted that in its rate making functions it is not bound by any particular formula or combination of formulas (e. g., F. P. C. Br. p. 27, n. 14; p. 37). This means, as applied to the instant case, that there is not a single obstacle to the allowance of the 8c attribution price in Petitioner's city gate rates.[39] Then next when

38 See Federal Administrative Procedure Act, Section 10(e) (5 U. S. C. § 1009 (e)) providing that the reviewing court shall "hold unlawful and set aside agency action, findings and conclusions found to be (1) arbitrary, capricious, an abuse of discretion, or otherwise not in accordance with law * * *."

39 See concurring Opinion of Commissioner Smith, R. 13091 [R. V 2306].

we observe the Commission's line of reasoning in its recent *Phillips* Opinion,[40] and particularly the position being urged by the Commission in the Court of Appeals (D. C.) in the same case,[41] recognizing the crucial and key importance of price and price increases as a necessary and legally permissible tool of conservation, it is patently clear that the Commission's action in the instant case is sheer whim or caprice.

The Commission seeks to extricate itself from its dilemma (F. P. C. Br. p. 37). Referring to the Commission's own *Phillips* decision it states: "It was there held that the Act [Natural Gas Act] *excludes* from [Federal Power] Commission regulation INTERSTATE sales made in the course of production or gathering,"[42] and then goes on to say "we are not concerned here with such sales but with how Federal authority may be applied to sales conceded to be within the jurisdiction of the Federal Power Commission." What does this mean? It obviously means that if the Kansas Commission's conservation price is embodied in the price paid to a producer, in an INTERSTATE sale, which is made either at the well mouth or at the end of the gathering lines, the Commission would fully recognize that price in the city gate rate of the gas-pipeline-company purchaser (which it does in the case of Petitioner's purchased gas in the instant case). But where the same Kansas Commission wellhead price, as a matter of sheer geography, is similarly involved in an INTERSTATE sale at a city gate, the Commission will

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40 Re Phillips Petroleum Company, F. P. C. Docket No. G-1148, Opinion No. 217 (Pet. Br. pp. 49-51).

41 State of Wisconsin, et al v. Federal Power Commission (C. A., D. C.), No. 11247 (Pet. Br. pp. 59-60).

42 This, of course, refers to sales made either at the wellhead or at the end of the gathering lines.

treat the Kansas Commission Order as a nullity. The Commission has failed to analyze or justify the rationale by findings in its Opinion (R. 13047-13048).

Not only does the Commission decision violate the Administrative Procedure Act, Section 10(e)[43] but it likewise violates Section 8(b) of such Act.[44] It is clear under Section 8(b) that the Commission must include findings and conclusions on relevant issues of administrative discretion. The House Judiciary Committee in its explanation of the provisions of Section 8(b) (House Rep. No. 1980, 79th Cong., 2nd Sess., reprinted in Leg. Hist. Vol. p. 273) said:

> It should also be noted that the relevant issues extend to matters of administrative discretion as well as of law and fact. This is important because agencies often appear to determine only whether they have power to act rather than whether their discretion should be exercised or how it should be exercised. Furthermore, without a disclosure of the basis for the exercise of, or failure to exercise, discretion, the parties are unable to determine what other or additional facts they might offer by way of rehearing or reconsideration of decisions.

Nowhere does the Commission say *why* they should, in their discretion, treat the Kansas Commission Order as a nullity with respect to Petitioner's produced gas in the Kansas Hugoton Field (assuming for the purpose of this argument only that the Commission is not legally

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43 See supra, n. 38, p. 22.

44 The Administrative Procedure Act, Section 8(b) [5 U.S.C. § 1007 (b)], provides in part as follows: "* * * All decisions * * * shall become part of the record and include a statement of (1) findings and conclusions, as well as the reasons or basis therefor, upon all the material issues of fact, law, or discretion presented on the record; * * *." [Emphasis supplied.]

bound to give full force and effect to the Kansas Commission Order). The Commission has not or cannot argue that it is legally bound to ignore such order and treat it as a nullity.

Petitioner has previously set forth the failure of the Commission to disclose the reasons justifying its treatment of the Kansas Order as a nullity in respect to Petitioner's production in the Kansas Hugoton Field (Pet. Br. pp. 65-73, particularly pp. 67-68). Among pertinent inquiries logically addressable by this Court to the Commission's action are these:

1. Has the Commission found that the Kansas Commission Order imposes, or attempts to impose, an embargo against the movement of its gas in Interstate commerce?

2. Has the Commission found that the Kansas Commission's Order in any wise discriminates against interstate commerce in the gas produced in the Kansas-Hugoton field?

3. Has the Commission found that the Kansas Commission Order does not safeguard an obvious state interest?

4. Has the Commission found that the local interest at stake in the Kansas Commission Order does not outweigh whatever national interest there might be in the province of the state restriction?

5. Has the Commission found that the public interest is served, and, if so, why and to what extent by its refusal to recognize the Kansas Commission's 8 cent Order as a floor in fixing Petitioner's rates?

It is submitted that in its treatment of the Kansas Commission Order the arbitrariness of the Commission's action, its abuse of discretion and its failure to make findings in answer to the inquiries indicated above warrant the reversal of its Order (Administrative Procedure Act, Sections 8(b) and 10(e); Pet. Br. pp. 65-73).

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CITATIONS

Cases:

Bluefield Water Works & Imp. Co. v. *Public Service Commission*, 262 U. S. 679 — 12

Colorado Interstate Gas Co. v. *Federal Power Commission*, 324 U. S. 581 — 6, 11

Colorado Interstate Gas Co. v. *Federal Power Commission* (C. A. 10) No. 4541 (decided October 29, 1953) — 9, 12, 14–15, 16, 17

Federal Power Commission v. *Hope Natural Gas Co.*, 320 U. S. 591 — 6, 8, 9, 10, 11, 13, 14

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Hope Natural Gas Co., 3 F. P. C. 150 — 13

Mississippi River Fuel Corp. v. *Federal Power Commission*, 163 F. 2d 433 — 12, 14, 16

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Panhandle Eastern Pipe Line Co. v. *Federal Power Commission*, 324 U. S. 635 — 6, 13

Pennsylvania Water & Power Co. v. *Federal Power Commission*, 193 F. 2d 230, affirmed, 343 U. S. 414 — 6, 14

Safe Harbor Water Power Corp. v. *Federal Power Commission*, 179 F. 2d 179, certiorari denied, 339 U. S. 957 — 9, 14

United Railways v. *West*, 280 U. S. 234 — 6

Statutes:

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Sec. 5 (a) — 20

Sec. 19 (b) — 21

In the Supreme Court of the United States

OCTOBER TERM, 1953

No. ——

FEDERAL POWER COMMISSION, PETITIONER

v.

NORTHERN NATURAL GAS COMPANY, ET AL.

CROSS-PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE EIGHTH CIRCUIT

On September 28, 1953, respondents herein, the State Corporation Commission of the State of Kansas and Northern Natural Gas Company, filed petitions for writs of certiorari (Nos. 381 and 382, respectively) in the above-entitled proceedings seeking review of certain parts of the judgment rendered by the United States Court of Appeals for the Eighth Circuit which were decided adversely to them. The Federal Power Commission has filed a brief in opposition to the granting of these petitions.

The Acting Solicitor General, on behalf of the Federal Power Commission, prays that in the event this Court grants the petitions for writs of certiorari in Nos. 381 and 382 or either of them,

a cross-writ of certiorari be issued to review that additional portion of the judgment of the United States Court of Appeals for the Eighth Circuit as indicated by the statement of question presented, *infra*.

OPINIONS BELOW

The Opinion and Order of the Federal Power Commission (R. V 2257–2314) is reported at 95 P. U. R. (N. S.) 289. The opinion of the United States Court of Appeals for the Eighth Circuit (R. VI 2433–2497) is reported at 206 F. 2d 690.

JURISDICTION

The judgment of the Court of Appeals was entered on July 20, 1953 (R. 2498). By Order of Mr. Justice Clark dated October 8, 1953, the time within which to file this cross-petition was extended to and including November 17, 1953. The jurisdiction of this Court is invoked under 28 U. S. C. 1254 (1) and Section 19 (b) of the Natural Gas Act.

QUESTION PRESENTED

Whether the Court of Appeals could lawfully set aside a rate of return fixed by the Federal Power Commission based upon substantial financial data, without finding that the rate of return is confiscatory.

STATUTES INVOLVED

The pertinent provisions of the Natural Gas Act are set forth in the Appendix, *infra*, pp. 20–21.

STATEMENT

A full statement of the facts involved and of the proceedings before the Federal Power Commission and before the Court of Appeals has been set forth in the brief of the Federal Power Commission in opposition in Nos. 381 and 382, to which the Court is respectfully referred. The facts pertinent to the issue raised by this cross petition may be summarized as follows:

One of the elements on the basis of which the Federal Power Commission allowed to Northern Natural Gas Company an over-all rate increase of about $5,000,000 was its conclusion, after examination of all the available evidence in the record, that a 5½% rate of return on Northern's rate base of about $140,000,000 would produce a fair and reasonable end result (R. V. 2271). This rate of return would allow Northern, after the payment of the 2.55% interest on its long term debt constituting 56% of its capitalization, a return of 9.25% on its common stock equity which after deducting ½% cost of flotation, leaves a net return of 8.75% to the equity owner.[1] Under Northern's past practice of paying out 62.7% of its earnings as dividends and trans-

[1] The common stock equity which constitutes the remaining 44% of Northern's capitalization, includes, the par value of the common stock, premiums thereon and capital and earned surpluses.

ferring the balance of 37.3% to surplus, this return of 8.75% represents a dividend yield of 5.49% (R. V 2274).

The Commission reached the conclusion that a return of 8.75% and a dividend yield of 5.49% to Northern stockholders would be a fair and reasonable end result upon an examination of investors' requirements as evidenced by the earnings-price ratios and dividend yields on common stocks of the only seven natural-gas companies (including Northern) whose common stocks are actively traded on recognized stock exchanges (see R. I 187–188), and upon a study of similar data with respect to Northern's own common stock (R. V 2273). It found that an over-all return of 5½% would provide a yield on Northern's equity in excess of the average earnings-price ratio and yield since 1945 of the seven natural-gas companies and higher than the average earnings-price ratio and yield for 1951 for these companies as well as for Northern.

While the Court of Appeals affirmed the order of the Federal Power Commission in all other respects, it reversed the Commission's conclusion as to the sufficiency of a 5½% rate of return, and remanded with directions to make additional findings and conclusions on this score (R. VI 2482–2492). The fundamental basis for this ruling was the court's belief that the Commission's reasoning was inadequate because certain factors

discussed by the Commission in the rate-of-return portion of other decisions were not referred to in the rate-of-return section of this decision.

SPECIFICATION OF ERROR

The Court of Appeals erred in reversing the determination by the Federal Power Commission that a 5½% rate of return would be just and reasonable and in remanding the case to the Commission with directions to make additional findings and conclusions on that issue.

REASONS FOR GRANTING THE WRIT

In this case, the Federal Power Commission has determined that 5½% would be a just and reasonable rate of return to Northern primarily on the basis of financial materials relating to Northern and other companies engaged in the natural gas business. The court below reversed the Commission's conclusion because the Commission's opinion did not contain specific findings as to Northern's markets and adequacy of its gas reserves, etc., and further because there was testimony in the record which would support a higher rate of return. This holding not only conflicts in principle with decisions of the Court of Appeals for the Tenth and District of Columbia Circuits, but it disregards the controlling decisions of this Court.

1. "The question for the courts when a rate order is challenged is whether the order viewed

in its entirety and measured by its end results meets the requirements of the Act." *Colorado Interstate Gas Co.* v. *Federal Power Commission,* 324 U. S. 581, 605; *Federal Power Commission* v. *Hope Natural Gas Co.,* 320 U. S. 591, 602; *Panhandle Eastern Pipe Line Co.* v. *Federal Power Commission,* 324 U. S. 635, 649; *Pennsylvania Water & Power Co.* v. *Federal Power Commission,* 343 U. S. 414, 424. In determining a fair and reasonable rate of return, the Commission is required to allow a return sufficient to maintain the financial integrity of the company. It must allow for service on the long-term indebtedness, reasonable dividends on the stock, and a sufficient margin of earnings for transfer to surplus. Cf. *United Railways* v. *West,* 280 U. S. 234, 251–252. The return to the stockholder "should be commensurate with returns on investments in other enterprises having corresponding risks," so as to maintain the company's "credit and to attract capital." *Federal Power Commission* v. *Hope Natural Gas Co., supra* at 603; *Colorado Interstate Gas Co.* v. *Federal Power Commission, supra; Panhandle Eastern Pipe Line Co.* v. *Federal Power Commission, supra* at 650. This standard is by no means vague or meaningless, for it is of a financial nature "resting on stubborn facts" (*Colorado Interstate Co.* v. *Federal Power Commission,* 324 U. S. 581, 605), even if it may be difficult, if not impossible, to cast it into a legalistic formula (cf.

concurring opinion of Black, Douglas and Murphy, JJ, in *Federal Power Commission* v. *Natural Gas Pipeline Co.*, 315 U. S. 575, 607).

The 5½% over-all return fixed by the Commission complied fully with these standards. It provided an allowance of 2.55% representing the actual cost on Northern's long-term debt and a return of 9.25% on common stock which, adjusted for financing charges of ½%, gave a net return to the equity owner of 8.75% (R. V 2274). This would have permitted the continuance of Northern's past practice of transferring 37.3% of these earnings to surplus and left for distribution as dividends to the stockholders enough to yield 5.49% on the book value of their stock, a figure comparing favorably with the yields of similarly situated natural-gas companies (R. V 2274).

The adequacy of this yield of 5.49% was corroborated by the fact that it approximated the past yields on Northern's own stock; Northern's average yield during the past five years had been 5.6% and its latest 5.1% (R. V 2274). In addition, the net return of 8.75% corresponded more than favorably with the indicated investment requirements of persons seeking to purchase natural gas stock as shown by reference to common stocks of seven natural-gas companies actively traded on recognized stock exchanges, which included common stocks of natural-gas companies relied on by

Northern (R. V 2274).[2] Finally the Commission double-checked the return allowed by it against Northern's own past performance and against the average earnings-price ratio, *i. e.*, the accepted indicator of return requirements of investors desiring to purchase natural-gas company stocks. Here again the Commission relied not only upon the figures prepared by its own staff but also upon the somewhat higher ones submitted by Northern (R. V 2273).[3] All tests coincided in showing that the 5½% figure would give Northern a return somewhat in excess of the average of the past five years and considerably above the figures for the Spring of 1951, which were the latest ones available. Plainly, therefore, the 5½% return allowed by the Commission complied with the test that it be high enough to maintain the company's credit and to attract new capital.[4] It follows that the over-all rate of return fully protected the investor's interest as well as Northern's financial integrity (*Federal Power Commission* v. *Hope Natural Gas Co.*, 320 U. S. 591, 602).

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[2] This return averaged 8.1% during the period from 1946 to the conclusion of the hearings. It amounted to 7½% on April 30, 1951, the latest available figure (R. 2273).

[3] These figures were 8½% for the 1946 to 1951 average and 7.3% on May 31, 1951 (R. 2273).

[4] The financial data did not disclose that Northern was subject to any particular vulnerability. Nor was any claim made to that effect. As a matter of fact, Northern's gas reserves are somewhat larger than those of comparable natural-gas companies (R. IV 1918). And the low interest rate it pays on its long-term indebtedness also attests to its financial health (cf. R. IV 1715–1731).

2. (a) In reversing the Commission's conclusion as to rate of return, the court below disregarded the established standards for review of such rate determinations. Since rate determinations are largely based on financial standards, difficult to cast into legal formulae and requiring pragmatic adjustments (*Federal Power Commission* v. *Hope Natural Gas Co.*, 320 U. S. 591, 602), the critical consideration is the end result, *i. e.*, the final impact of the order, not the method or the theory upon which any one of its elements is based. See cases cited at p. 6, *supra*. Hence, judicial review is confined to a determination whether the end result is just and reasonable or confiscatory. Moreover, since the order is the product of expert judgment, it "carries a presumption of validity"; the mere circumstance that it is challenged does not render it suspect. To the contrary, the party who seeks to challenge it has to bear the "heavy burden" that the consequences of the order—not the Commission's method of reaching it—are unjust and unreasonable. *Federal Power Commission* v. *Hope Natural Gas Co.*, 320 U. S. 591, 602.[8]

[8] In *Safe Harbor Water Power Corp.* v. *Federal Power Commission*, 179 F. 2d 179, 201 (C. A. 3), certiorari denied, 339 U. S. 957, the Court of Appeals properly applied these standards by refusing to interfere with the determination of a rate of return in the absence of a showing that the order was clearly confiscatory. See, also, *Colorado Interstate Gas Co.* v. *Federal Power Commission* (C. A. 10) No. 4541 (decided October 29, 1953).

The court below while professing to follow this standard of review (R. VI 2490) totally disregarded it. Instead of affording the rate order the presumption of validity and imposing upon respondent the heavy burden of showing that the end result was confiscatory, the court reversed the Commission's conclusion as to rate of return on the ground that the Commission has not sufficiently explained why it considered 5½% a reasonable rate of return, other than stating that it provides a yield to the common stock owners of Northern comparable or greater than those yielded by other natural-gas companies (R. VI 2491). And while the court's opinion goes out of its way to enumerate material in the record pointing to a higher rate of return, the court did not find that these circumstances showed convincingly that the rate order was unjust and unreasonable; it merely found that these factors militated against the order. In other words, the court below, in violation of the standards of judicial review set out in the *Hope* case, held that the rate order was suspect because challenged by contradictory evidence, that Northern had been relieved of its burden of showing convincingly that the end result was unjust and unreasonable and that, consequently, the order had to be set aside, unless it showed positively on its face not only that its end result was just and reasonable, but also that it was based on reasoning acceptable to the court.

(b) Moreover, the Commission's findings were adequate to support its conclusion. As already indicated, *supra,* pp. 4, 7–8, the Commission's conclusion was not, as the court below erroneously asserted, based merely on a comparison of dividend yields of similarly situated natural-gas companies. In addition, since the determination of rates is based fundamentally upon stubborn financial standards (*Colorado Interstate Gas Co.* v. *Federal Power Commission*, 324 U. S. 581, 605) and is supposed to take into consideration the investor's appraisal of the return necessary to maintain the financial integrity of the enterprise (*Federal Power Commission* v. *Hope Natural Gas Co.*, 320 U. S. 591, 603), the Commission properly predicated its decision on the very basic tests the investor uses in determining whether or not he should invest his funds in the corporation, *viz,* the return on the investment and the dividend yield. Northern's financial expert conceded that dividend yields and earnings-price ratios, which are the only readily available objective evidence [6] of common stock capital cost, of necessity had to be used and be given weight, subject to the necessary adjustments (R. II 676–677).[7] They become even

[6] He termed the dividend yield the basic evidence (R. II 675).

[7] The adjustments suggested by the witness were threefold. He felt that more consideration should be paid to inflationary tendencies (R. II 650–666, 717), thus trying to revert to the reproduction cost theory rejected by this Court. Second, he felt that regardless of the stubborn facts of

more conclusive when checked back, as here, against the company's own past experience. Since the Commission was using financial data which itself take into consideration the composite of Northern's problems and those of companies having corresponding risks, it was not necessary to discuss the specific problems confronting Northern (cf. R. VI 2489) in the absence of an assertion that Northern's status was so unique as to make untrustworthy any comparison with other natural-gas companies.[8]

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actual purchases by investors, the special risks of the natural-gas companies required that they be given a net return of about 140% of the earning ratio of electric utilities (R. II 689–692, 717–718). We submit that this totally speculative argument is not entitled to much worth. Finally, the witness argued that the Commission should permit a return so high as to permit Northern to compete for capital with non-regulated business enterprises (R. II 681–682, 728, 735–736). This is at odds with the long-established holding of this Court that a regulated utility is not entitled to returns commensurate with those realized or anticipated by non-regulated enterprises. *Bluefield Water Works & Imp. Co.* v. *Pub. Serv. Commission*, 262 U. S. 679, 692.

[8] It will be noted that Northern itself felt that it was comparable with three other natural-gas companies and that the Commission used this comparison to cross-check the reasonableness of the rate determined by it (R. V 2273). See also *supra*, p. 8, fn. 4.

Other courts of appeals have recognized the sufficiency of financial materials as a criterion for the rate of return. Cf. *Mississippi River Fuel Corp.* v. *Federal Power Commission*, 163 F. 2d 433, 436–437 (C. A. D. C.); *Colorado Interstate Gas Co.* v. *Federal Power Commission*, (C. A. 10) No. 4541 (decided October 29, 1953); and see *infra*, pp. 16 to 18.

The court below stressed the circumstances that earlier opinions of the Federal Power Commission and of this Court contained considerable discussions of the individual problems of the several regulated companies. The instant opinion of the Federal Power Commission, however, explains in detail how the 5½% rate of return determined by it to be just and reasonable would be split between interest on the long term debt, the cost of financing, and the net return to the stockholders, that the latter compares favorably with Northern's own past history and with the requirements of investors "in other enterprises having similar risks," and that it permits Northern to transfer more than one-third to surplus and still leave a satisfactory dividend yield. We submit that this detailed discussion of the actual financial impact of the rate order on the company is far more informative than were the opinions of the Federal Power Commission in *Hope Natural Gas Co.*, 3 F. P. C. 150, 185–186, and *Panhandle Eastern Pipe Line Co.*, 3 F. P. C. 273, 285–286, upheld by this Court in *Federal Power Commission* v. *Hope Natural Gas Co.*, 320 U. S. 591, and *Panhandle Eastern Pipe Line Co.* v. *Federal Power Commission*, 324 U. S. 635. There the Commission merely stated (see 3 F. P. C. at 186 and 285–286–287) that it considered that 6½% was a fair return without showing what net rate of return or dividend yield this gross return would allow to the stockholders and how this compared with the

requirements of persons seeking to invest in the industry.

(c) The court below apparently was greatly concerned by the circumstance that the 5½% return was the lowest allowed to any natural-gas company, and evidently felt that this involved a "pioneering change in its rate-of-return concept" requiring more elaborate explanation (R. VI 2490, 2492; see also the concurring opinion of Johnsen, J., at R. VI 2497). The fact is, however, that the Commission in this case introduced no innovations in its approach to and determination of the rate of return. The Commission here relied on substantially the same kind of evidence, drawn from the same kind of rate-of-return studies, which has uniformly been held sufficient to support the Commission's findings on rate of return. *Federal Power Commission* v. *Natural Gas Pipeline Co.*, 315 U. S. 575; *Federal Power Commission* v. *Hope Natural Gas Co.*, 320 U. S. 591; *Mississippi River Fuel Corp.* v. *Federal Power Commission*, 163 F. 2d 433 (C. A. D. C.); *Safe Harbor Water Power Corp.* v. *Federal Power Commission*, 179 F. 2d 179 (C. A. 3), certiorari denied, 339 U. S. 957; *Pennsylvania Water & Power Co.* v. *Federal Power Commission*, 193 F. 2d 230 (C. A. D. C.), affirmed, 343 U. S. 414; *Colorado Interstate Gas Co.* v. *Federal Power Commission*, (C. A. 10) No. 4541 (decided October 29, 1953). In the *Colorado* case, *supra*, where, as here, the allowance of a rate of return

of less than 6% was used as a basis for the contention that the Commission has changed its approach to the determination of a fair rate of return, the Tenth Circuit said:

> While the rate of return of 5¾% is lower than any rate heretofore established which has been called to our attention, that in itself is not suspect nor may we overturn it merely because we as the trier of the facts might have established a higher rate. From the record we cannot say that a rate of return of 5¾% properly computed is unreasonable and therefore confiscatory.

So, here too the 5½% return allowed by the Commission was not unreasonable. This return provided an allowance covering Northern's actual cost of 2.55% of servicing its long-term indebtedness, representing 56% of its total capitalization. This, together with the 9.25% found by the Commission to be a fair return on the common stock, representing the remaining 44% of Northern's compensation, gives the 5½% figure.*

---

*This is illustrated by the following tabulation:

Capitalization Ratios	
56% bonds x 2.55% cost of borrowed money	1.43%
44% common x 9.25% return on common	4.07%
	5.50%

A calculation such as this one appearing in the Commission's opinion was misunderstood by the Court of Appeals as representing the starting point for the rate-of-return determination and a mathematical derivation of the 5½% return, whereas in fact the tabulation is merely a means of charting the end result.

3. The decision below conflicts in principle with decisions of the United States Courts of Appeals for the Tenth and District of Columbia Circuits upholding rate orders of the Federal Power Commission based upon financial data similar to those utilized in the instant case. *Colorado Interstate Gas Co.* v. *Federal Power Commission,* (C. A. 10) No. 4541 (decided October 29, 1953);[10] *Mississippi River Fuel Corp.* v. *Federal Power Commission,* 163 F. 2d 433, 436–437 (C. A. D. C.). In each of these cases, the Commission's determination as to rate of return was based essentially on comparative yields, earnings-price ratios and interest rates as indicative of the investors' requirements and their appraisal of the utility, and in each, the Commission's determination was approved by the reviewing court.

In *Mississippi River Fuel Corp.* v. *Federal Power Commission,* 163 F. 2d 433, at 437, the Court of Appeals for the District of Columbia Circuit stated:

> About half of the capital of this petitioner is represented by 2½% long-term notes and the other half by equity capital. From the standpoint of the cost-of-capital rule, the 6% rate of return allowed would meet the obligation of the 2½% notes and allow

[10] Since this opinion has not yet been reported, mimeographed copies are being submitted to the Clerk for distribution to the Court. The section dealing with the rate of return begins on page 12.

> about 9½% on the common stock and surplus. The record does not furnish any other statistical test of the end result of the allowance on the equity capital. * * *
>
> Upon this evidence we cannot say that the rate of return allowed by the Commission was beyond the limit of its power, either as unreasonable, insufficient, or unsupported by substantial evidence.

And again in the very recent decision in *Colorado Interstate Gas Co.* v. *Federal Power Commission,* the Court of Appeals for the Tenth Circuit affirmed a 5¾% rate of return,[11] saying:

> * * * it is clear to us that no consideration was given by the Commission to factors other than the financial history of nine natural gas companies subject to the Commission's jurisdiction, whose common stock was held by the public, and seven natural gas companies, whose common stock was traded on recognized exchanges, and the data with respect to Colorado's outstanding securities, its earnings and financial requirements.
>
> * * * * *
>
> It would seem that the history and experience of other successful companies engaged in the production, transportation

[11] In this case, the weighted cost of the company's long-term indebtedness representing 54% of total capitalization was 3.25%, its preferred stock (3.6% of total capitalization) had a dividend rate of 6% and the net return on common stock equity was only 8.45%.

> and sale of goods [sic: "gas"?] would furnish the best guide as to what was fair and adequate. * * *
>
> * * * * *
>
> We believe that the experience of other comparable gas utility companies, having a sound financial structure and long experience of successful operation, is a better criteria by which to gauge and determine the adequacy and fairness of rate of return than that of railroads, power transmission companies or other like utilities engaged in other fields and under other conditions and circumstances, or the rate of return on Government bonds or industrial bonds in unrelated enterprises. We do not say that such factors are not proper for consideration but on the other hand failure to give them weighty consideration does not in our opinion constitute reversible error on the record before us in light of the factors that were considered in this case.

This statement of the Tenth Circuit applies with particular force here since the seven natural-gas companies referred to by that court are the same companies, the financial data of which was relied on by the Commission here.[12]

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[12] The Tenth Circuit referred to the opinion below in the instant case as "distinguishable," but without stating in what respect.

CONCLUSION

The question presented by this conditional cross-petition is of substantial importance. We are not requesting a grant of certiorari unconditionally, irrespective of the disposition of the other petitions for certiorari, because of the desirability of bringing this litigation to an early conclusion. It is respectfully requested, therefore, that this cross-petition for a writ of certiorari be granted if the petitions for certiorari in Nos. 381 and 382 are granted.

ROBERT L. STERN,
Acting Solicitor General.

WILLARD W. GATCHELL,
General Counsel,
Federal Power Commission.

NOVEMBER 1953.

APPENDIX

The Natural Gas Act (52 Stat. 821, 15 U. S. C. 717 *et seq.*) provides in pertinent part:

* * * * *

SEC. 5. (a) Whenever the Commission, after a hearing had upon its own motion or upon complaint of any State, municipality, State commission, or gas distributing company, shall find that any rate, charge, or classification demanded, observed, charged, or collected by any natural-gas company in connection with any transportation or sale of natural gas, subject to the jurisdiction of the Commission, or that any rule, regulation, practice, or contract affecting such rate, charge, or classification is unjust, unreasonable, unduly discriminatory, or preferential, the Commission shall determine the just and reasonable rate, charge, classification, rule, regulation, practice, or contract to be thereafter observed and in force, and shall fix the same by order: *Provided, however,* That the Commission shall have no power to order any increase in any rate contained in the currently effective schedule of such natural-gas company on file with the Commission, unless such increase is in accordance with a new schedule filed by such natural-gas company; but the Commission may order a decrease where existing rates are unjust, unduly discriminatory, preferential, otherwise unlawful, or are not the lowest reasonable rates.

* * * * *

SEC. 19. * * *.

(b) Any party to a proceeding under this Act aggrieved by an order issued by the Commission in such proceeding may obtain a review of such order in the circuit court of appeals of the United States for any circuit wherein the natural-gas company to which the order relates is located or has its principal place of business, or in the United States Court of Appeals for the District of Columbia, by filing in such court, within sixty days after the order of the Commission upon the application for rehearing, a written petition praying that the order of the Commission be modified or set aside in whole or in part. A copy of such petition shall forthwith be served upon any member of the Commission and thereupon the Commission shall certify and file with the court a transcript of the record upon which the order complained of was entered. Upon the filing of such transcript such court shall have exclusive jurisdiction to affirm, modify, or set aside such order in whole or in part. No objection to the order of the Commission shall be considered by the court unless such objection shall have been urged before the Commission in the application for rehearing unless there is reasonable ground for failure so to do. The finding of the Commission as to the facts, if supported by substantial evidence, shall be conclusive. * * *

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